immediate budget problem is one of excessive supplies, the general policy options are to reduce domestic supplies either by restricting production or by expanding exports. The effectiveness of export expansion policies is limited by the sheer size and complexity of international markets and by competition. Thus, restricting production is a more plausible option for bringing supplies in line with demand in order to reduce price support outlays.

Dairy farmers, unlike crop farmers, produce mainly for the domestic market. Although economic recession has dampened the demand for milk and dairy products, high price supports have continued to cause dairy surpluses with their attendant budget problems. Dairy farmers have increased milk production, by expanding herds and improving productivity per cow, to the point where annual milk production exceeds commercial use by 10 percent. This has not led, however, to any mechanism to control milk production such as exists for grains and cotton.

BROAD REDUCTION STRATEGIES

In this section two broad strategies for reducing price support outlays are examined: (1) reducing the level of federal support for crops and milk; and (2) restricting domestic crop production. The 1984-1988 savings from these strategies are displayed in Table VI-2.

Reducing the Level of Federal Support

Three possible ways of reducing federal support are: eliminating deficiency payments, capping the level of the farmer-owned reserve, and reducing the dairy price support level. Each of these three options, however, would reduce federal outlays at the expense of farmers' incomes.

Eliminate Deficiency Payments. In the mid-1960s, U.S. policy began to shift away from high domestic price supports and rigid supply controls, allowing domestic grain and upland cotton prices to adjust gradually to world price levels. From the mid-1960s to the early 1970s, farmers were assisted in making this adjustment through special payments averaging $3 billion annually. In 1973, these were replaced by deficiency payments for wheat, feed grains, upland cotton, and rice.

Altogether, in crop years 1974 through 1980, about $2.5 billion of deficiency payments were made. About $1.2 billion of deficiency payments were made for 1981 crops in fiscal year 1982 because of higher target prices and low crop prices, and because most farmers participated in the programs.

17-390 O - 83 - 11

TABLE VI-2. BUDGET SAVINGS FROM BROAD REDUCTION STRATEGIES IN AGRICULTURAL PRICE SUPPORT PROGRAMS (In billions of dollars)

Strategy	1984	1985	1986	1987	1988	Cumulative Five-Year Savings
Reducing the Level of Federal Support						
Eliminate Deficiency Payments						
Budget Authority	--	--	1,935	3,540	3,580	9,055
Outlays	1,935	3,540	3,580	3,380	3,065	15,500
Cap the Farmer-Owned Reserve						
Budget Authority	--	--	110	--	--	110
Outlays	110	--	--	--	--	110
Reduce the Level of Dairy Price Support a/						
Budget Authority	--	--	-985	-290	60	-1,215
Outlays	-985	-290	60	200	1,135	120
Restricting Crop Production						
Budget Authority	--	--	450	5,490	1,660	7,600
Outlays	450	5,490	1,660	1,485	985	10,070

a. Minus sign indicates an increase as compared with the baseline.

Deficiency payments will reach about $1.5 billion for 1982 crops. These payments are highly concentrated among larger farmers and are of small economic consequence to most others. In crop year 1981, about 6 percent of participating producers received about 57 percent of total deficiency payments under the wheat, feed grain, and upland cotton programs--an average payment of $10,024 to each of these producers as compared with $551 for all other participants.

One can argue that deficiency payments have largely fulfilled their function. Eliminating these payments starting with 1984 crops would save $5.5 billion in fiscal years 1984 and 1985. Crop farmers' incomes would still be cushioned by other provisions of existing commodity programs--the farmer-owned grain reserve, crop loans, and acreage diversion payments. On the other hand, deficiency payments are estimated at nearly 10 percent of crop farmers' gross cash incomes in the 1983 crop year. Thus, in years of especially large commodity surplus, such as 1981-1983, the grain reserve, crop loans, and diversion payments may not provide farmers with adequate income support.

Cap the Farmer-Owned Reserve. The reserve was established to help farmers extend their marketing period in times of surplus production. It was also seen as a way to protect consumers from shortages and precipitously rising prices. The reserve has helped to even out supplies over time and to dampen grain price fluctuations. It has been used more and more as a supply control tool, and thus is now larger than necessary to protect against production shortfalls. At the end of the 1982 crop year, the reserve will contain about 3.5 billion bushels of wheat and feed grains--roughly equal to one year's exports. In fiscal year 1983, it will require outlays of $0.6 billion for storage payments. In addition to its budgetary costs, the reserve causes prices to rise in a period of large surpluses, stimulating production and exacerbating the supply/demand imbalance.

Capping the reserve at current levels would mean that about 600 million bushels of 1982 and 1983 crop grains would not be entered into the reserve. Overall savings from smaller loans and storage payments would be $1.8 billion in 1983 and 1984. Net budget savings would be much less, however, since farmers, no longer having access to the farmer-owned reserve, would most likely place the same amount of grain under nonrecourse loans. When those loans matured farmers would probably forfeit their grain to the government since market prices are expected to be lower than the loan rates plus interest. Under these conditions, the government would acquire grain and would have to pay storage and handling costs, which would reduce the budget savings from smaller reserve loans and storage payments. The net budget savings from capping the reserve would thus be about $210 million in 1983 and 1984. Most of these savings would occur because the nonrecourse loan rate is lower than the reserve loan rate. For farmers, this would mean a lower price for part of their grain.

Reduce the Level of Dairy Price Support. The dairy price support program has increased farm milk prices at the expense of consumers and taxpayers, but it has also helped to stabilize the dairy industry and provide an assured supply of milk and dairy products. In the past three years, however, milk price supports have been at a level that has contributed to a sharp expansion of milk production. Milk production in 1982 was nearly 10 percent greater than in 1979. The increase in milk production far exceeded the growth in consumption. As a result, in 1981 and 1982, the commercial supply of milk exceeded commercial use by about 10 percent, with all the excess purchased by the federal government at an annual average cost of almost $2 billion.

The 1982 Reconciliation Act authorized a slight reduction of dairy support prices for 1983 and 1984 and gave the Secretary of Agriculture the authority to impose assessments on milk marketings. These actions were intended to induce dairy farmers to decrease milk production and to help defray the government's cost of purchasing surplus dairy products.

The federal assessment on dairy farmers represents a per unit tax on each hundredweight of milk sold, thus transferring income from dairy farmers to the government. Since neither the support price nor the pricing system is directly affected by this tax, consumer prices will remain unchanged for at least the short term. Even though the net price received by dairy farmers is reduced by the amount of the tax, this is not expected to reduce milk production significantly. Large grain crops currently ensure relatively low feed costs, and cattle prices are not high enough to encourage the culling of dairy cow herds. Consequently, milk supply and demand are not projected to balance until after 1987. This means that government surplus purchases will continue at high levels and burdensome stocks will expand, even though assessment revenues will reduce price support outlays.

One optional approach to balancing supply and demand would be to eliminate the assessment on dairy farmers and, instead, reduce support prices so that consumers would benefit. In order to reduce support outlays sufficiently to offset the loss of potential assessment revenues in fiscal year 1983, the support price would need to be lowered sharply from the current level. This would have no net budget impact but would represent a large income loss to dairy producers and might destabilize the dairy economy, causing increased consumer costs later on. Alternatively, by decreasing the support price in five increments of $0.50 per hundredweight every six months beginning April 1, 1983, a gradual and more even reduction in milk production and increases in consumption could be achieved that would lead to smaller government purchases. Nevertheless, price support outlays would be larger than under the assessment scheme, by about $985 million in 1984 and $290 million in 1985.

Restricting Crop Production

Under current law the Secretary of Agriculture can restrict crop production by withholding program benefits from farmers who do not reduce planted acreage, and in addition by paying farmers for diverting acreage. Both of these tools are being used for 1983 crops: farmers must reduce planted acreage by a specified percentage from 1982 base levels, and for a portion of this reduced acreage they will receive diversion payments intended to compensate them for forgone income. These programs were implemented with the expectation that they would reduce production, boost prices, and decrease price support outlays.

Such voluntary acreage reduction programs, while consistent with the long-term policy objective of giving farmers greater freedom in managing their businesses, have a limited capacity to reduce production. There are two reasons for this. First, many farmers typically choose not to participate and may even increase acreage in the expectation that prices will be higher. Second, farmers who do participate tend to remove their least productive cropland, and may even take steps to increase yields on cropland they plant. The usual result is that the net reduction in total planted acreage is less than the acreage removed under the program, and average yields are higher, so that production does not decline in proportion to the acreage removed. Consequently, under current excess supply conditions, these programs cannot be expected to bring supplies into line with demand over the short term.

An alternative approach to restricting production would be mandatory acreage reduction. This policy--which would require legislation--would give the Secretary the authority to limit 1984 planted acreage to some proportion of each farmer's base acreage. Farmers would still be eligible for nonrecourse loans, the farmer-owned grain reserve, and deficiency payments. Enforcement procedures and penalties would have to be established.

As compared with the present policy, programs mandating acreage reduction of 25 percent for the 1984 wheat and corn crops would:

- Increase season average wheat and corn prices by 10 to 15 percent;

- o Reduce 1984 ending corn and wheat stocks by 25 and 10 percent, respectively; and

- o Reduce 1984 and 1985 outlays by $5.9 billion (see Table VI-2). The savings would come from loan repayments, principally farmer-owned reserve loans, smaller reserve storage payments, and reduced deficiency payments.

Since stocks would be drawn down to meet demand in excess of production, 1984 ending stocks would be closer to adequate levels. This would improve crop farmers' prospects for 1985.

Higher grain prices would have very small impacts on retail food prices and on overall consumer prices. Manufacturers might experience a decline in sales to farmers in 1984, but this would probably be reversed as higher farm prices and incomes, along with improved prospects for 1985, contributed to increased demand for production inputs. In foreign trade, higher U.S. crop prices could cause a slight reduction in export demand, especially if the dollar remained strong relative to other currencies. To the extent that this led to increased production in other exporting nations, it could intensify competition in world markets and possibly dampen the increase in U.S. crop prices.

Mandatory acreage reduction would mean at least a temporary increase in government intervention in farming. This policy, however, would perhaps be more equitable in that all crop farmers would share in the adjustment. Unlike under voluntary programs, it would eliminate the prospect that participants might lose and nonparticipants gain. In the past, crop farmers generally were given the opportunity to vote via referendums whether they favored acreage allotments and marketing quotas. Mandatory acreage reductions for 1984 could be put to the same test.

TARGETED REDUCTION STRATEGIES

Three targeted reduction strategies are discussed in this section, and their savings are displayed in Table VI-3. These savings are relatively small, however, compared with those discussed above.

Eliminate the Wool and Mohair Program. The National Wool Act of 1954 authorized payments to farmers on marketings of shorn wool, unshorn lambs, and mohair. Payments are at a rate approximating the difference between the support price established in the law and the national average price received by farmers. The program was enacted as a measure of national security and general economic welfare, because shorn wool was

TABLE VI-3. BUDGET SAVINGS FROM TARGETED REDUCTION STRATEGIES IN AGRICULTURAL PRICE SUPPORT PROGRAMS (In millions of dollars)

Options	1984	1985	1986	1987	1988	Cumulative Five-Year Savings
Eliminate the Wool and Mohair Program						
Budget Authority	--	65	76	85	92	318
Outlays	65	76	85	92	96	414
Eliminate the Honey Price Support Program						
Budget Authority	--	--	33	36	38	107
Outlays	33	36	38	40	41	188
Place the Peanut Program on a No-Net-Cost Basis						
Budget Authority	--	--	38	38	38	114
Outlays	38	38	38	38	38	190

considered an essential and strategic commodity. The objective was to encourage annual domestic production of 300 million pounds of shorn wool.

About $1.3 billion has been paid to farmers since the inception of the program; the amount in 1982 was $42 million. Even so, domestic wool production has declined by more than one-half since 1954 and is now about 100 million pounds a year. The program has been in direct conflict with the reality of declining lamb and mutton consumption and rising use of synthetic fibers. Eliminating this program would save about $414 million over the 1984-1988 period.

The elimination of program payments would reduce farmers' cash receipts from the marketing of wool and mohair by about a third. Federal payments, however, are only about 10 percent of the total cash receipts that farmers receive from the sale of sheep, lambs, and wool. These payments are made to just 80,000 farmers and average only $400 per farmer.

Consequently, the elimination of payments would be of small economic consequence to most farmers.

Eliminate the Honey Price Support Program. Honey producers' incomes are supported through government loan and purchase activities operated by the CCC. For the past several years, the price support loan has been set at 60 percent of the honey parity price--the minimum required by law. Prior to the 1980 honey marketing year, market prices remained above the loan rate, and while there was loan activity the government acquired no honey. In 1980 the parity index increased sufficiently to raise the loan rate to almost the market price, and in 1981 the loan rate increased further so that it exceeded the market price. As a result, in 1981 the government acquired 37 million pounds of honey at a cost of about $27 million.

The price support program results in higher prices not only for domestic producers but for foreign producers as well. About 200 million pounds of honey are produced annually in this country--about 75 percent of domestic consumption. Imports make up the difference. Imports have increased nearly 30 million pounds in the past two years in response to higher support price levels. Honey imports, most of which are from Mexico, China, Canada, and Argentina, are not subject to import quotas and bear only a small duty.

Eliminating the honey program would benefit consumers by allowing prices to fall below support levels. Domestic producers would suffer some loss of income from lower prices, and imports would likely fall. The government would save the expense of acquiring honey, estimated to be $190 million in 1984-1988.

Place the Peanut Program on a No-Net-Cost Basis. The peanut program supports producers' prices and incomes through nonrecourse loans and poundage quotas which restrict the quantity of peanuts eligible for preferential loan rates. Peanuts produced in excess of the poundage quota are supported at a substantially lower loan rate. The peanut program is similar in many respects to the tobacco program. Peanut producers, like tobacco producers, could be assessed in order to assure that the government does not incur any realized losses.

Estimated savings from fees would be $190 million in 1984-1988. The fees would recover the costs of storage, transportation, and losses on nonrecourse loans.

CONCLUDING COMMENTS

Two broad strategies have been outlined for reducing crop price support programs. Restricting production through mandatory acreage controls would increase government intervention in agriculture, in contrast to recent policy trends. On the other hand, eliminating deficiency payments would be consistent with the policy transition.

Changing world economic conditions could affect the relative merits of these two budget reduction strategies. A fairly rapid improvement in the world economy would stimulate U.S. farm exports--thus reducing excess supplies, raising farm prices, and reducing federal outlays. This would lessen the adverse consequences of eliminating deficiency payments, and intensify the negative price and income effects of restricting production. Alternatively, a slow rate of growth in export demand would mean continued low prices and big outlays. It would exacerbate the adverse effect of eliminating deficiency payments, but would minimize the negative effects of restricting production.

In the short term, there appears to be little prospect of any significant increase in export demand. From this viewpoint, mandatory acreage controls for 1984 offer a means to reduce supplies, increase farm prices, and reduce outlays. This policy would save about $5.5 billion in 1984 and 1985, similar to the savings from eliminating deficiency payments. Unlike the elimination of deficiency payments, however, mandatory acreage controls would not reduce crop farmer's gross cash incomes.

An argument can be made for longer-term acreage adjustment policies that would retire land from production for several years. The outsize crops of recent years suggest that the present program for managing supply may be inadequate, particularly in light of the poor outlook for exports. Restricting land under cultivation until demand can grow into balance with world supplies might be less costly to the federal budget than are the present annual attempts to control production on all of U.S. cropland.

The dairy price support program poses another policy dilemma. Currently, dairy farmers are taxed to help defray part of the costs of the price support program. These revenues reduce price support outlays, but do not result in lower prices and increased consumption. Government surpluses are expected to grow even though part of their acquisition and disposal costs are paid by farmers. The policy dilemma is that a practicable alternative approach such as gradually reducing the level of price support would benefit consumers but would most likely cause outlays to increase over the next two years.

CHAPTER VII. NONDEFENSE DISCRETIONARY SPENDING

More than one-half of all federal budget accounts are in the category "nondefense discretionary spending." Despite its vast range--it encompasses all or part of 16 of the 19 budget functions--spending in this category totaled only $137 billion in 1982, or less than one-fifth of all net federal budget outlays. This was a sharp drop from the 1980 level, when nondefense discretionary programs accounted for nearly one-fourth of all outlays. Off-budget outlays for these programs added $17 billion to 1982 expenditures.

Nondefense discretionary spending ranges from international affairs to energy, education and training, and transportation. It also includes all of the expenses of operating the federal government, except for defense-related agencies. The programs included in this category are classified as "discretionary" because--unlike the entitlement programs described in Chapters III-VI--spending in these areas is fixed directly by the Congress, generally through the annual appropriations process.

In this chapter, nondefense discretionary programs are grouped into the following subcategories:

- **Grants to State and Local Governments.** This subcategory includes most aid that flows from the federal government to states and localities to be used for purposes specified by the federal government. Transportation, education and training, community and regional development, and natural resources and environmental assistance make up the bulk of programs in this subcategory. 1/

1. As noted in earlier chapters, the Office of Management and Budget also classifies as grants to state and local governments several large entitlement programs that provide benefits to individuals, because the funds are distributed first to other governments before being passed through to the eventual beneficiaries. Such benefit-payment grants--among them, Aid to Families with Dependent Children, Medicaid, and child nutrition programs--are dealt with in Chapters IV and V and are therefore not included in the grants totals in this chapter. The General Revenue Sharing and Title XX Social Services block grant programs are also considered entitlements for the purpose of this

- **Assistance to Business and Commerce.** This includes subsidies for specific industries--such as low-interest loans to farmers, operating subsidies for shipowners, and low-interest loans to subsidize exports--as well as general aid to commerce.

- **Benefits and Services for Individuals.** This includes programs that provide direct federal financing for such benefits as veterans' health care and lower-income housing assistance.

- **Infrastructure, Environment, and Related Services.** This includes direct federal spending for such services as environmental regulation, the national parks system, the work of the Bureau of Land Management and the Army Corps of Engineers, and the air traffic control system, which are available directly or indirectly to all citizens.

- **Research and Development.** This includes all research and development expenditures for purposes other than national defense.

- **Aid to Foreign Governments and International Organizations.** This includes all bilateral and multilateral economic and military assistance to foreign governments as well as U.S. payments to international organizations, such as the United Nations.

- **Other Government Operations.** This includes the costs of operating all three branches of the federal government, except for the Department of Defense and for those agencies and bureaus that provide federally administered services or conduct research and development.

BUDGET HISTORY AND PROJECTIONS

Spending for nondefense discretionary programs declined slightly between fiscal years 1980 and 1982, and is expected to increase in 1983 to just

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report and are covered in Chapter V. Finally, several state and local grants that are discretionary appropriated programs but that provide fully earmarked benefit payments for individuals--such as lower-income housing assistance--are counted in this chapter as direct federal benefits for individuals. For all these reasons, the state and local grants totals reported in this chapter will not agree with figures reported in other sources.

above the 1980 level--representing a substantial reduction over those three years, after adjusting for inflation. CBO's baseline projection assumes that beginning in 1984 spending in these programs will grow at about the same rate as inflation.

Recent History, 1980-1982

The first session of the 97th Congress, acting on proposals from the Reagan Administration, reduced funding for numerous nondefense discretionary programs and completely eliminated others. As a result, on-budget nondefense discretionary spending increased only slightly between 1980 and 1981, and declined in 1982 to below the 1980 level (see Table VII-1). Most of the spending growth that did occur over these two years was in benefits and services to individuals, research and development, and other government operations, although spending increased slightly for foreign aid as well. Spending for the other three nondefense discretionary subcategories combined fell by about $10 billion between 1980 and 1982, with the sharpest reduction occurring in state and local grants. Because of these cuts, total nondefense discretionary spending decreased by 18 percent in real terms between 1980 and 1982, and declined from 24 percent of net on-budget federal expenditures to 19 percent.

The Current Situation

After two years of little or no spending growth, outlays for nondefense discretionary programs are expected to increase somewhat between 1982 and 1983, but they will remain well below the 1980 level after adjusting for inflation. On-budget expenditures for the nondefense discretionary spending category as a whole are expected to rise to $145 billion in 1983, reflecting increases in all subcategories except state and local grants and assistance to business and commerce, which are expected to continue to decline. Between 1980 and 1983, total on-budget nondefense discretionary spending will grow by only $4 billion, leaving expenditures 16 percent below the 1980 level in real terms and shrinking total nondefense discretionary spending to 18 percent of the federal budget.

Baseline Projections, 1984-1988

CBO's baseline projections assume that funding for nondefense discretionary spending programs will increase from the 1983 levels at a rate sufficient to keep up with projected increases in the costs of the goods and services financed. On this basis, total on-budget expenditures for these

TABLE VII-1. FEDERAL OUTLAYS FOR NONDEFENSE DISCRETIONARY SPENDING (In billions of dollars)

Subcategory	Actual 1980	Actual 1982	Estimated 1983	Baseline Projection 1984	1985	1986	1987	1988
Unified Budget Outlays								
State and Local Grants a/	52	45	44	47	50	52	54	56
Assistance to Business and Commerce	9	7	7	8	9	9	9	9
Benefits and Services for Individuals	23	25	28	28	30	32	34	35
Infrastructure, Environment, and Related Services	19	18	20	21	22	22	22	23
Research and Development	15	16	17	18	18	18	19	20
Aid to Foreign Governments and International Organizations	8	8	9	10	10	11	11	11
Other Government Operations	15	17	19	20	20	20	21	21
Civilian Agency Pay Raises b/	N/A	N/A	1	2	3	5	7	9
Subtotal	141	137	145	153	162	169	177	184
Off-Budget Outlays	14	17	17	15	16	19	17	17
Total, Unified and Off-Budget Outlays	155	154	162	168	178	188	194	201

a. Includes only nonentitlement grants. Entitlement grants are described in Chapters IV-V.

b. Reflects outlay increases associated with projected comparability pay raises for civilian-agency employees.

programs would grow to $153 billion in 1984 and to $184 billion by 1988. This inflation-adjusted baseline is used to measure the impact of the further spending reductions identified in this chapter.

DEFICIT REDUCTION STRATEGIES

For the 1984 budget resolution, the Congress could approach nondefense discretionary spending in either of two ways, or through some combination of them. On one hand, the Congress could derive funding totals for this category by applying broad guidelines to all or most of this group of programs as a whole. Alternatively, funding totals could be developed by making spending assumptions about the individual programs and aggregating the effects of those assumptions. The organization of the rest of this chapter reflects these two approaches, first discussing general spending guidelines, and then examining examples of program-specific cutbacks.

GENERAL BUDGET GUIDELINES

This section describes three possible general budget guidelines for the nondefense discretionary spending category. These guidelines are summarized in Table VII-2.

Increase Funding by Less Than the Inflation Rate

One means of achieving savings in nondefense discretionary programs relative to the CBO baseline would be to allow funding to increase, but at some rate less than the anticipated rate of inflation. For example, the Congress could permit funding for appropriated accounts to rise by 2 percent per year from 1983 levels--about half the expected rate of inflation over the next five years--while permitting anticipated federal pay comparability increases to go forward. 2/ Such a guideline would permit outlays for nondefense discretionary spending to increase by more than $30 billion by 1988, but would achieve savings of nearly $1 billion in 1984 and more than $8 billion in 1988 relative to the CBO baseline, which is fully adjusted for inflation. Under this guideline, nondefense discretionary programs would decline in real terms by 2 percent between 1983 and 1988, and by 18 percent over the 1980-1988 period.

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2. Options for reducing federal employee compensation costs are discussed in Chapter VIII.

TABLE VII-2. SAVINGS FROM GENERAL BUDGET GUIDELINES FOR NONDEFENSE DISCRETIONARY SPENDING (In billions of dollars)

Budget Guideline	1984	1985	1986	1987	1988	Cumulative Five-Year Savings
Increase Funding by 2 Percent per Year						
Budget Authority	2.2	4.5	6.9	9.5	11.8	34.9
Outlays	0.8	2.4	4.2	6.2	8.3	21.9
Freeze Funding at 1983 Levels						
Budget Authority	5.0	10.2	15.5	21.0	26.4	78.1
Outlays	2.1	6.0	10.6	15.6	20.7	55.0
Decrease Funding by 2 Percent per Year						
Budget Authority	7.8	15.9	24.1	32.5	41.0	121.3
Outlays	3.4	9.6	17.0	25.0	33.1	88.1

Freeze Funding at 1983 Levels

One obvious general budget approach would be to hold appropriations for the nondefense discretionary category at the 1983 level--permitting funding increases only to pay for federal pay adjustments. Under this guideline, outlays--or actual expenditures--would still rise by $18 billion between 1983 and 1988, with about half of that increase resulting from projected pay adjustments, and the other half resulting from expenditure growth that is already built into law, such as spending associated with the recently enacted increase in the motor fuels tax. Under this approach, annual savings relative to the CBO baseline would amount to about $2 billion in 1984, and almost $21 billion by 1988. This strategy would result in a 9 percent reduction in nondefense discretionary spending in real terms between 1983 and 1988, and a 24 percent real-dollar reduction over the entire 1980-1988 period.

Reduce Funding Below the Base-Year Level

If further savings were desired in nondefense discretionary spending programs--at the cost of still greater erosion in the level of services provided--funding for 1984 and thereafter could be reduced below the base-year level. As one example, 1984 funding for this category could be fixed at 2 percent below the 1983 level--except for anticipated federal pay increases--with funding for subsequent years reduced by an additional 2 percent annually. Such a strategy would achieve outlay savings of $3.4 billion relative to the inflation-adjusted baseline in 1984, rising to more than $33 billion by 1988. Adopting this guideline would result in a 30 percent real-dollar decline in spending for nondefense discretionary programs as a whole over the 1980-1988 period.

TARGETED REDUCTION STRATEGIES

Whatever general guidelines are employed in developing nondefense discretionary funding totals for the 1984 budget resolution, numerous program-specific decisions will have to be made, usually as part of the appropriations process. Indeed, the budget resolution itself could be constructed in such a "bottom up" manner--aggregating assumptions regarding eventual appropriations actions for individual programs.

The remainder of this chapter presents targeted budget reduction strategies and examples of specific spending cuts that might be applied to each of the seven program clusters identified at the outset of the chapter. 3/

State and Local Grants

The federal government provides grants to states and localities that help finance a wide array of public services. Several large entitlement grants, including the principal health care and income support programs for the poor, are discussed in Chapter V. Nonentitlement grants--examined below and summarized in Table VII-3--include state highway construction and repair grants, mass transit assistance, community and economic development aid, elementary and secondary education grants, employment and training aid, and pollution abatement assistance. In some instances, grants are earmarked to fund increased services for certain disadvantaged groups

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3. Examples of deficit reductions that could be achieved by establishing or increasing user fees for public services are discussed in Chapter IX.

17-390 O - 83 - 12

TABLE VII-3. FEDERAL OUTLAYS FOR NONENTITLEMENT STATE AND LOCAL GRANTS (In billions of dollars)

Program	Actuals 1980	Actuals 1981	Actuals 1982	Estimated 1983
Federal-Aid Highways	9	9	8	8
Elementary, Secondary, and Vocational Education	6	7	6	6
Community and Regional Development Aid	7	6	5	5
Employment and Training Assistance	9	8	4	4
Urban Mass Transit	3	4	4	4
Wastewater Treatment	4	4	4	3
Social Services	3	2	2	2
Health Grants	2	2	2	2
Energy Assistance	2	2	2	2
All Others	7	8	8	8
Total	52	52	45	44

or to finance specific services not generally available. In other cases, the federal funds merely increase the level of already-available state and local services. Funding for nonentitlement grants was cut back sharply during the 97th Congress, reducing outlays from $52 billion in 1980 to $45 billion in 1982, with a further $1 billion decline expected in 1983.

Spending for state and local grants could be reduced still further either by shifting responsibility for selected programs to state and local governments or by reducing funding for less needy areas or populations. Such cutbacks would lower federal outlays, but they would place additional financial strains on states and localities. Because these governments are suffering the consequences of the current recession and earlier funding reductions, many jurisdictions would have difficulty replacing federal funds, at least in the short run. To the extent that states and localities increased their own revenue-raising efforts to compensate for federal cutbacks, the total cost of government at all levels would remain unchanged, although the distribution of those costs would be altered.

The examples of grant reductions discussed below and summarized in Table VII-4 cover transportation, education, community and economic development, environmental services, the administration of justice, and social services.

Require Cost-Sharing for Future Funding Increases. The federal role in financing public services could be reduced by requiring that states and localities share the burden of funding increases in selected grants. This approach would ensure that increased federal funding went only for those services valued sufficiently to induce jurisdictions to contribute a share of any additional costs. On the other hand, many governments, because of their weakened fiscal condition, would be hard pressed to meet the matching requirements--potentially leaving the additional federal assistance out of reach of those states and localities most in need.

One example of such an action would be to increase funding for selected state and local grants by one-half the expected rate of inflation, on the condition that recipient jurisdictions match the added federal funds with a like amount of their own resources. If this strategy was adopted beginning in 1984 for the principal education, employment and training, nutrition, and community development programs, for example, savings relative to the full-inflation baseline would amount to about $150 million in that year, rising to $1.5 billion by 1988. These savings are calculated assuming that all states and localities would match the federal funding increases. If any jurisdictions failed to provide matching funds, federal savings would be greater, but the amount of additional services provided would be less.

Reduce and Refocus Federal Highway Funding. The federal government--in partnership with states--finances the construction and repair of highways and bridges. The federal contribution was $8.4 billion in 1982 and will grow to $15.6 billion by 1988 if current policies are continued--primarily because of the recently enacted 5-cents-per-gallon motor fuels tax increase, 4 cents of which is to be used for highways. State expenditures for these same roads totaled $6.1 billion in 1982, of which $1.6 billion was required to match the federal contribution.

Over the years, the federal-state partnership in financing the construction of highways has grown to include more locally oriented segments of the nation's road network, such as beltways and other local routes. As a result, today, only two-thirds of federal highway funds are spent for the two most nationally oriented road systems (the Interstate and Primary systems), compared with 90 percent just 15 years ago.

Substantial savings could be achieved by gradually limiting the federal highway program to its original emphasis on intercity arteries. The largest

TABLE VII-4. BUDGET SAVINGS FROM REDUCTIONS IN STATE AND LOCAL GRANTS (In millions of dollars)

Options	1984	1985	1986	1987	1988	Cumulative Five-Year Savings
Require Cost-Sharing for Future Funding Increases						
Budget Authority	490	790	1,150	1,510	1,880	5,820
Outlays	150	400	750	1,110	1,470	3,880
Reduce Interstate Highway Funding						
Budget Authority	3,000	3,000	3,000	3,000	3,000	15,000
Outlays	510	2,070	2,520	2,670	2,760	10,530
End Federal Aid for Urban and Secondary Roads						
Budget Authority	1,450	1,450	1,450	1,450	1,450	7,455
Outlays	250	975	1,195	1,275	1,365	5,060
Reduce Federal Mass Transit Aid						
Budget Authority	1,200	1,220	1,240	1,290	1,340	6,290
Outlays	900	960	1,040	1,140	1,260	5,300
End Airport Assistance for Facilities Not Serving National Needs						
Budget Authority	440	435	450	450	465	2,240
Outlays	90	285	375	420	450	1,620
End Assistance for Financially Self-Sufficient Airports						
Budget Authority	190	185	195	195	200	965
Outlays	40	125	160	185	195	705

(Continued)